

City and County of San Francisco

Office of the Controller - City Services Auditor

OFFICE OF THE SHERIFF:

The Sheriff Is Entitled to
Additional Commissions From Its
Telephone Services Provider for the
Inmate Welfare Fund

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CITY AND COUNTY OF SAN FRANCISCO
OFFICE OF THE CONTROLLER

Ed Harrington
Controller

Monique Zmuda
Deputy Controller

March 16, 2007

Michael Hennessey, Sheriff
Office of the Sheriff
City Hall, Room 456
San Francisco, CA 94102

Dear Sheriff Hennessey:

The Office of the Controller presents its report concerning the audit of the Inmate Welfare Fund (Fund) managed by the Office of the Sheriff (Sheriff). The Fund provides money for certain services and for educational, vocational, and recreational programs provided to inmates in the jails run by the City and County of San Francisco (City).

The Sheriff appropriately accounted for Fund revenues and expenditures; however, we determined that the provider of inmate telephone services, Public Communication Services, Inc. (PCS), may owe up to \$1.9 million in retroactive commissions and late interest charges to the Sheriff because PCS did not exercise the "Most Favored Customer" clause in its contract. The clause states that should PCS grant higher commission rates to a similar institution under a similar telephone services agreement; it should grant the Sheriff such higher rates and any greater benefit as of the commencement of such agreement with the other entity and reimburse the Sheriff for past under-compensated commission rates, plus interest. We identified two other jail facilities where PCS granted higher commissions than it is paying to the Sheriff.

The Sheriff can also improve the management and administration of the inmate telephone services and inmate commissary services contracts, which are the main sources of Fund revenues. The Sheriff did not use a competitive bidding process to select its inmate telephone services provider and could have obtained higher commission rates. Furthermore, the telephone services contract and commissary contract were not approved by the Board of Supervisors as required by the San Francisco Charter.

Finally, we had concerns about the inmate telephone system's ability to accurately capture and maintain adequate phone records and whether PCS accurately calculated and paid commissions to the Sheriff.

The Sheriff's responses are attached to this report. The Controller's City Services Auditor-Financial Audits will follow up with the Sheriff on the status of the recommendations made in this report.

Respectfully Submitted,

Ed Harrington
Controller

INTRODUCTION

BACKGROUND

Section 4025 of the California Penal Code (Penal Code) provides that each county may maintain an inmate welfare fund, and requires that the fund be used for the benefit, education, and welfare of the inmates confined in county jails. The Office of the Sheriff (Sheriff) of the City and County of San Francisco (City) administers the City's Inmate Welfare Fund (Fund).

In accordance with the Penal Code, and as required by Section 10.100-329 of the San Francisco Administrative Code, the Sheriff uses the Fund to provide educational, vocational, and recreational programs to inmates. The Sheriff administers grant and contract agreements with several non-profit organizations to provide these services. In addition, the Sheriff uses the fund to provide certain medical, dental, and legal supplies to inmates, to maintain facilities, and to purchase equipment for inmate use.

Fund revenues come from various sources. As required by the Penal Code, the Sheriff deposits the following revenues into the Fund:

- Commissions and fees received from a provider of telephone services to inmates.
- Commissions received from a food service company that sells commissary, such as confectionary and hygiene products, to inmates.
- Interest earned on deposits in the Fund bank account.

The Sheriff also deposits into the fund all cash contraband, donations, approved fundraising monies, vending machine profits, and monetary gifts it receives for inmate welfare purposes.

SCOPE AND METHODOLOGY

At the request of the Sheriff, we conducted this audit to determine whether the Inmate Welfare Fund was properly administered between July 1, 2003, and June 30, 2005.

We determined whether adequate internal controls existed over the financial operations of the Fund, and whether the Sheriff properly recorded and deposited all the revenues it received for the Fund. We also determined whether the Sheriff correctly authorized and recorded expenditures from the Fund. In addition, we determined whether the Sheriff administered the Fund in compliance with applicable state and city regulations.

We assessed the reasonableness of telephone and commissary contractor payments by reviewing applicable contract terms and the contractor's procedures for recording, summarizing, and reporting gross revenues and commissions to the Sheriff. Additionally, we tested, on a sample basis, the revenues reported based on supporting documentation provided by the contractors.

We also assessed the reasonableness of the Sheriff's expenditures from the Fund. We reviewed, on a sample basis, related grants and contracts and tested the accuracy of expenditures by verifying supporting documentation such as accounting records, time sheets, and vendor invoices.

We did not review any other funds established for the inmates, such as the Inmate Trust Fund or the Inmate Welfare Revolving Fund.

THE SHERIFF SHOULD COLLECT ADDITIONAL COMMISSIONS FROM THE TELEPHONE SERVICES PROVIDER

The telephone service provider, Public Communication Services, Inc. (PCS), underpaid commissions to the Sheriff because PCS did not increase its commission rates according to contract terms. As a result, we estimate that PCS may owe the Sheriff up to \$1.9 million for retroactive commissions and late interest charges.

The Sheriff May Be Due Higher Commission Rates

PCS may owe as much as \$1,921,589 in retroactive commissions and late charges because it did not increase commission rates commensurate with higher rates given to other custody facilities under the "Most Favored Customer" clause in the 1999 and 2006 contracts with the Sheriff.

The clause requires PCS to increase the Sheriff's commission rates or pay any greater or additional benefit equal to those provided to any other custody facility located in the United States for similar telephone services and contractual arrangement on the date provided to the other facility. The clause further states that the Sheriff should also notify PCS if it becomes aware that other PCS customers receive higher commission rates. As a result, PCS would raise the commission rate and reimburse the Sheriff for past under-compensated commission rates, including interest, based on the date the rates were offered to the other facility. According to the undersheriff, PCS did not inform the Sheriff of any such instance.

We determined that PCS entered agreements with other jail facilities for higher commission rates during the Sheriff's contract term. Specifically, PCS entered an inmate telephone service contract in June 2000 with a county jail facility in Florida, and paid 45 percent commissions on all debit call revenues and 43 percent for all other call types. PCS also contracted with another California county, in 2003, to provide inmate telephone services and to pay commissions of 45 percent of all call revenues. In contrast, for the period from June 2000 through March 2006, PCS paid the Sheriff just 33 percent of revenues in commissions, which represents an average of all the Sheriff's call service types and rates.

According to PCS's chief financial officer, the contract with the Sheriff is not similar to any other facility because of the variations in call volume, mix, and rates as well as system configurations specific to the Sheriff's contractual arrangement. However, we concluded that the services offered were not sufficiently different to warrant the wide

disparity in commission rates. Therefore, PCS should have increased the Sheriff's commission rates to a level commensurate with those offered to other facilities under the "Most Favored Customer" clause.

Using the commission rates paid by PCS to the other two counties, we estimate the Sheriff may be due an additional \$1,309,535 in retroactive commissions for the period of June 2000 through March 2006. Furthermore, we calculate that PCS owes interest of \$612,054 for not paying the additional commissions when due, based on the current personal loan interest rate available in the San Francisco area.

RECOMMENDATION

The Office of the Sheriff should take the following actions to collect funds due from Public Communication Services, Inc.:

1. Work with the Office of the City Attorney to bill and collect from PCS the \$1,921,589 in retroactive commissions and late interest charges, under the "Most Favored Customer" contract clause for the period of June 2000, through March 2006. Determine if there are additional amounts owed for months subsequent to March 2006.

THE SHERIFF NEEDS TO IMPROVE THE ADMINISTRATION OF ITS REVENUE CONTRACTS

The Sheriff recorded Inmate Welfare Fund revenues of \$2,068,787, and expenditures of \$2,101,954, during the audit period¹. The Sheriff properly managed the receipt, recording, and depositing of revenues to the Fund and correctly authorized and recorded expenditures from the Fund. However, the Sheriff needs to make improvements in the administration of its inmate telephone services and commissary contracts, which are the main sources of revenue for the Fund.

The Sheriff did not solicit competitive bids for the inmate telephone services contract in accordance with the San Francisco Administrative Code (Administrative Code). In addition, the Sheriff did not submit the inmate telephone services and commissary contracts to the Board of Supervisors (Board) for approval as required by the San Francisco Charter (Charter). Finally, the Sheriff incorrectly deposited \$66,437 of commissary commissions into the City's General Fund instead of depositing these amounts into the Fund as required by the California Penal Code.

¹ See Appendix for details by fiscal year.

Competitive Solicitation Process Not Used to Select a Telephone Service Provider

In 1999, the Sheriff entered a five-year contract with PCS to provide telephone services and equipment at the City's jails. The contract expired in April 2004; however, PCS continued to provide services under a verbal agreement with the Sheriff until January 1, 2006, when the Sheriff signed a new contract with PCS. Both contracts were entered without undergoing a competitive process.

A Sheriff staff member, who negotiated and signed the 1999 contract, was informed by the Sheriff that a competitive bidding process was not required. Additionally, a deputy city attorney informed the Sheriff that city regulations did not require competitive bidding for this specific type of contract because it did not involve expenditure of city money. The staff member conducted a brief telephone survey of several providers and found they did not provide the requisite services. Since the Sheriff's intent was to offer inmates the lowest possible rates, including the option to make debit card calls, it selected PCS, the only carrier that provided that option.

For the 2006 contract, the staff member was again informed by the Sheriff that the contract was not required to be competitively bid. However, the Sheriff did not make any inquiries to determine whether other vendors offered comparable services. The Sheriff's specific phone call requirements, however, should not prevent the Sheriff from conducting a competitive bidding process because calling rates and other requirements can be included in the competitive bid process.

The advantages of using a competitive bid process was shown where we identified another California county that received significantly better terms when it solicited bids for its inmate telephone services contract in 2001. That county awarded a three-year contract to a PCS competitor and received a \$250,000 one-time execution fee with a \$100,000 annual renewal fee as well as the greater of \$700,000 annual commissions or 51.50 percent of gross revenues. The Sheriff, however, only received an annual bonus of \$5,000 and was paid average commissions of 33 percent² of gross revenues with no annual minimum for the 1999 contract. We reviewed the other county's contract and considered it to be sufficiently similar to the Sheriff's contract with PCS.

Competitive bidding ensures that the Sheriff obtains the best contract terms possible and that the process of selecting contractors is transparent, diligent, and fair. Additionally, a competitive solicitation process should have been used because of the large amount of

²PCS pays the Sheriff varying rates of commission depending on the call type. PCS paid the Sheriff total commissions averaging 33 percent of total gross revenues for the period from June 2000 through March 2006.

revenues received by the contractor. PCS earned approximately \$13 million for the six years from 1999 through 2005.

Board of Supervisors Approval Not Obtained for Significant Contracts

The Sheriff did not submit its inmate telephone services and commissary services contracts to the Board of Supervisors for approval in accordance with Section 9.118(a) of the Charter. The Charter requires Board approval for all contracts with anticipated revenue of \$1 million or more.

For its 1999 contract with PCS, the Sheriff received commissions of approximately \$4 million over 5 years. Therefore, the Sheriff should have obtained Board approval when revenues exceeded \$1 million. According to the undersheriff, Board approval for the PCS contracts was not obtained because the City Attorney had already approved it. However, according to the deputy city attorney involved in approving the contract, the issue of anticipated revenues was never disclosed to them. For the 2006 PCS contract, the Sheriff should anticipate receiving commissions exceeding \$1 million for the eight-year contract period and should accordingly seek the Board's approval.

The Sheriff also did not obtain board approval for its 2002 commissary services contract with Canteen Correctional Services (Canteen). The contract guaranteed a minimum annual commission of \$400,000 over the two-year contract term with the option to extend for an additional year. Since the Sheriff's records show that it received \$1,676,570 in commissions for the 2002 contract, it should have requested Board of Supervisor approval as soon as the actual revenues exceeded \$1 million.

Not All Commissary Commissions Deposited Into the Fund

From July 1, 2000, through March 31, 2006, the Sheriff incorrectly deposited \$66,437 of commissary commissions into the City's General Fund. Section 4025 of the California Penal Code (Penal Code) requires profits from commissary sales to be deposited into the Fund. However, the Sheriff deposited \$21,360 of the commissary commissions for the two-year audit period into the City's General Fund with an additional \$45,077 incorrectly deposited for the periods prior to, and following, the audit period.

Canteen Correctional Services's contract required it to pay 41.5 percent of net sales in commissions to the Fund, with an additional one percent to be paid to the General Fund. The undersheriff stated that there was a provision in the San Francisco Administrative Code that allowed the one percent to be deposited into the General Fund. Although Section 13.10 of the Administrative Code allowed the Sheriff to do so, the section was repealed effective June 30, 2000. Therefore,

commencing on July 1, 2000, the Sheriff should have deposited all commissary commissions into the Fund for the benefit of inmates.

Provisions in the Telephone Services Contract Not Enforced

There were numerous instances, including long-term service outages, late commission payments, inadequate software support and undocumented and unapproved subcontractor access to the phone system, where PCS did not comply with the 1999 contract requirements. For example, a Sheriff's staff member who oversees the phone system stated that there were several issues regarding a subcontractor's software support service and undocumented access to the system, which could have compromised data integrity. However, no substantial measures were taken by the Sheriff to resolve those concerns until the 2006 contract was signed.

Telephone System Service Not Consistently Reliable

In analyzing the commissions paid by PCS to the Sheriff, commissions averaged approximately \$585,000 annually for the audit period as compared to approximately \$775,000 annually for the two previous fiscal years under the same contract. Furthermore, there was no corresponding drop in inmate population. PCS explained that there were several service outages that may have affected phone services during that period; however, PCS did not provide any further clarification of these issues.

Also, in July 2004, PCS paid approximately \$17,000 less in commissions compared to an average of all months in the audit period. A PCS accounting manager explained the low revenues by referring to line problems and a programming issue after a new T-1 line was installed in July 2004, further highlighting system reliability issues. However, PCS offered no further explanation of these issues.

PCS Could Not Provide Reports Allowing Verification of Reported Revenues

PCS could not provide complete and accurate monthly reports detailing gross revenues collected and received from the Sheriff's inmate telephone services system. Section 9 of the 1999 Inmate Telephone Service Agreement requires that PCS provide a detail of all telephone activity upon request. PCS assured us that the system could provide the required reports; however, after several attempts, PCS could not provide us information from its system that would allow us to verify whether monthly gross revenues reported by PCS agreed to actual revenues generated by inmate calls.

RECOMMENDATIONS

The Office of the Sheriff should take the following actions to improve its administration of the Inmate Welfare Fund:

2. Solicit competitive bids for inmate telephone services in place of the 2006 contract with Public Communication Services (PCS). If the PCS contract is selected, obtain Board of Supervisor approval for the 2006 inmate telephone services contract.
3. Establish a policy that requires all significant contracts to undergo competitive bidding. Develop and implement guidelines specifying how contractors are selected and monitored.
4. Obtain Board of Supervisor approval for the commissary contract with Canteen Correctional Services, Inc.
5. Obtain Board of Supervisor approval for all contracts, contract amendments or modifications, with anticipated revenues over \$1 million, in accordance with San Francisco Charter requirements.
6. Transfer the \$66,437 in commissary commissions from the City's General Fund into the Inmate Welfare Fund for the period July 1, 2000, through March 31, 2006. Determine whether additional amounts should be transferred subsequent to March 2006.
7. Report and follow-up with the contractor on instances of non-compliance with contract terms, including phone service outages and system inconsistencies until issues are satisfactorily resolved.

We conducted this review according to the standards established by the Institute of Internal Auditors. We limited our review to those areas specified in the scope and methodology section of this report.

Staff: Kevin Baloca, Audit Manager
Katherine Buckley

Appendix

Sheriff's Inmate Welfare Fund Statement of Revenues and Expenditures and Changes in Fund Balance For Fiscal Years Ended June of 2004 and 2005

	June 30, 2004	June 30, 2005
<i>Revenues</i>		
PCS - Inmate Collect Calls	\$ 498,855	\$ 672,658
Canteen Commissions	407,966	442,483
SBC Pacific Bell - Long Distance	37,250	-
Interest	4,703	3,656
Confiscated/Contraband Money from Inmates	1,017	98
Miscellaneous	-	101
<i>Total Revenues</i>	<u>\$ 949,791</u>	<u>\$ 1,118,996</u>
<i>Expenditures</i>		
Professional & Specialized Services ¹	\$ 459,818	\$ 41,939
City Grant Programs ²	-	222,292
Permanent Salaries & Premium Pay	328,397	309,620
Construction of 5th Floor Recreation Area in CJ #8 ³	155,630	-
Other Materials & Supplies	117,688	119,335
Related Mandatory Fringe Benefits	65,988	76,162
Other Current Expenses	28,498	34,796
Materials & Supplies	22,674	38,981
Equipment Purchase	-	11,675
Services of Other Departments	21,201	7,221
Training & Employee Expenses	8,276	7,692
Maintenance Services	7,985	3,450
Overhead	5,890	-
Transportation	2,913	3,357
Fee License	286	190
<i>Total Expenditures</i>	<u>\$ 1,225,244</u>	<u>\$ 876,710</u>
<i>Net Change in Fund Balance</i>	<u>\$ (275,453)</u>	<u>\$ 242,286</u>
<i>Beginning Fund Balance</i>	<u>\$ 367,070</u>	<u>\$ 91,617</u>
<i>Ending Fund Balance</i>	<u><u>\$ 91,617</u></u>	<u><u>\$ 333,903</u></u>

Notes:

¹ The total amount paid for external service providers, under Professional & Specialized Services & City Grant Programs decreased by approximately \$195,000 from 2004 to 2005 mainly due to grant program award reductions.

² City Grant Programs were accounted for separately from Professional & Specialized Services in 2005.

³ Construction was completed in 2004.

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OFFICE OF THE SHERIFF RESPONSE TO THE AUDIT

City and County of San Francisco

OFFICE OF THE SHERIFF



Michael Hennessey
SHERIFF

415 - 554 - 7225

February 28, 2007
Reference No. 2007-04

Ed Harrington, Controller
City and County of San Francisco
City Hall Room 316
San Francisco, CA 94102

Dear Mr. Harrington:

Thank you to you and your staff for the extensive and thorough work on the audit of the Inmate Welfare Fund. We appreciate their efforts and the results. To the extent possible, we intend to follow the recommendations. Our first steps will be to contact the prisoner telephone services contractor and assess their willingness to comply with the recommendations listed below. Their response will, of course, determine our follow up to the audit.

Following are the list of audit recommendations and our responses:

- **Recommendation:** Work with the Office of the City Attorney to bill and collect from PCS the \$1,921,589 in retroactive commissions and late interest charges, under the "Most Favored Customer" contract clause for the period of June 2000, through March 2006. Determine if there are additional amounts owed for months subsequent to March 2006.

Response: Agree. We will confer with the City Attorney regarding the interpretation of "Most Favored Customer" and, with assistance from your staff, including access to the work papers they developed in making this recommendation, determine the extent to which the contractor owes us money. We will then work with the City Attorney to recover any funds owed.

OFFICE OF THE SHERIFF RESPONSE TO THE AUDIT

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- **Recommendation:** Solicit competitive bids for inmate telephone services in place of the 2006 contract with Public Communication Services (PCS). If the PCS contract is selected, obtain Board of Supervisor approval for the 2006 inmate telephone services contract.

Response: The process used by our department for the current contract was based on the advice of the City Attorney. The outcome of the first recommendation above will determine whether we re-bid the current contract before its expiration. There are certain operational issues involving other law enforcement agencies which would be impaired if we changed contractors immediately.

- **Recommendation:** Establish a policy that requires all significant contracts to undergo competitive bidding. Develop and implement guidelines specifying how contractors are selected and monitored.

Response: Agree. Unless we receive legal advice to take a different course of action, we always follow all City procedures and policies in our contracting processes.

- **Recommendation:** Obtain Board of Supervisors' approval for the commissary contract with Canteen Correctional Services, Inc.

Response: Agree. The commissary contract competitive bidding process is not completed. Once we finish negotiations with the vendor, we will submit the contract to the Board of Supervisors for approval.

- **Recommendation:** Obtain Board of Supervisors approval for all contracts, contract amendments or modifications, with anticipated revenues of over \$1 million, in accordance with San Francisco Charter requirements.

Response: Agree.

- **Recommendation:** Transfer the \$66,437 in commissary commissions from the City's General Fund into the Inmate Welfare Fund for the period July 1, 2000, through March 31, 2006. Determine whether additional amounts should be transferred subsequent to March 2006.

Response: Agree. We will work with the Controller's Office to recover these revenues from the General Fund.

OFFICE OF THE SHERIFF RESPONSE TO THE AUDIT

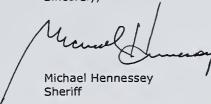
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- **Recommendation:** Report and follow-up with the contractor on instances of non-compliance with contract terms, including phone service outages and system inconsistencies until issues are satisfactorily resolved.

Response: Agree. We have assigned an additional staff person to the Sheriff's Bureau of Building Services who will be responsible for this monitoring. The position is currently temporary; we will seek to create this as a permanent position in the 2007-2008 budget.

Again, we appreciate your staff's assistance in these matters and look forward to a quick resolution of the outstanding recommendations. If you have any further questions or comments on this response, please contact Jean Mariani at (415) 554-4462.

Sincerely,



Michael Hennessey
Sheriff

cc: Jan Dempsey, Undersheriff
Jean Mariani, Assistant Sheriff
Kevin Lyons, Sheriff's Bureau of Building Services

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cc: Mayor
Board of Supervisors
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